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- Overseas aspects of personal taxation



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(a) Bill Mickelson (June 2015)

(45 mins)

You are a tax adviser working for Grandal LLP, a firm of ICAEW Chartered Accountants.

Bill Mickelson, his daughter Wilma and her husband-to-be Jorge are tax clients of your firm. Bill is the owner of a bicycle business. He started his business in 1996 when he inherited a workshop from his father which he still uses in his business. You have received an email from Bill (**Exhibit 1**).



assistant has had a short meeting with Wilma and Jorge and has left you some notes (**Exhibit 2**).

- 1 Reply to Bill's email explaining the capital gains tax implications for him of the sale and gift of his business assets to Wilma and the income tax liability in respect of the rental income.
- 2 Prepare briefing notes for a meeting with Jorge and Wilma which include:
 - advice for Jorge on his residency status in the tax year 2021/22 and the tax implications of the timing of the sale of his property in Barcelona;
 - an explanation and calculation of Wilma's income tax and capital gains tax liabilities for 2020/21 after taking into account any reliefs and elections available to her; and
 - advice for Wilma of the inheritance tax implications of the gift to her by her grandmother of the holiday home.

Total: 30 marks

Exhibit 1: Email from Bill

To: Tax Adviser
From: Bill Mickelson
Date: 5 June 2021
Subject: Retirement plans

I have been offered a job touring round the world as a mechanic with an international cycle team and I have decided to sell my business to my daughter, Wilma. I will leave for a two month trip to Australia on 1 August 2021. After I return from Australia I will be in the UK until the cycling season starts again in May 2022.

I need you to explain to me whether I have any tax to pay. The date of the sale has been agreed as 1 August 2021. I have set out below valuations of and information about my business assets and some notes of the terms I have agreed with Wilma:

Business assets of bicycle business

	Notes	Market value at 1 August 2021 £	Information
Retail building	1	130,000	Purchased in 2006 for £55,000
Workshop	2	250,000	Inherited in 1996 with probate value of £128,000
Goodwill	3	175,000	Created since 1996
Inventory	4	45,000	All purchased since January 2021
Plant and machinery	4	1,000	The tax written down value of plant and machinery is £1,000

Notes of terms agreed with Wilma

- (1) Wilma will eventually inherit the retail building when I die so I have agreed to gift it to her. As I will receive no cash from her for the retail building, I believe that this will save me tax.
- (2) I would like to retain ownership of the workshop. Wilma has agreed to pay me £6,000 for the first six months' rent in advance on 1 August 2021 and she will continue to pay six-monthly in advance. She will pay this £6,000 rent direct to a bank account in Australia which I recently opened. Therefore I believe that this amount will not be taxed in the UK.
- (3) On 1 August 2021 Wilma will pay me £175,000 for the goodwill of my business.
I cannot believe I would have to pay any tax on this amount received for goodwill as I have worked hard to build up the reputation of the business.
- (4) Wilma has agreed to pay me £1,000 for the plant and machinery on 1 August 2021. For the inventory, we agreed she will pay me three instalments of £15,000 with the first instalment due on 1 September 2021.

Exhibit 2: Notes from meeting with Wilma and Jorge

Jorge is a professional cyclist and was born in Spain where he is currently tax resident. Jorge and Wilma are getting married on 1 October 2021 in the UK. After the wedding, Jorge will retire as a professional cyclist and live in the UK working for Wilma in the bicycle business. Jorge's only stay in the UK since 6 April 2021 is a nine day visit to make the wedding arrangements. Jorge intends to settle in the UK and needs advice on his residency status. He owns a property in Barcelona, Spain. He is unsure whether to sell this property before or after his wedding on 1 October 2021.

In June 2015, Wilma's grandmother gifted a holiday home to Wilma which was valued at £445,000. Wilma decided to let out the holiday home for the first time in December 2020. The property was actually let out for 31 days during the period from 1 December 2020 to 31 March 2021 and Wilma received net rental income of £16,000 for this period. On 31 March 2021, in order to raise finance to buy her father's business, Wilma sold the holiday home for £485,000. Wilma would like us to confirm that because she did not actually buy the holiday home, she will not have any tax to pay on its sale.

Sadly Wilma's grandmother has just died and she has received a letter from her grandmother's executor asking for details of the gift of the holiday home. Wilma was very concerned that she would have tax to pay as a result of the gift and needs more information on this.

After buying her father's business, Wilma intends to invest in new plant and machinery and shop fittings and therefore projects that the business will, in the first 12 months to 31 July 2022, make a tax adjusted trading loss of £240,000 but that thereafter the business will make taxable profits in the year ending 31 July 2023.

Wilma does not intend to withdraw any money from the business. She will pay Jorge an annual salary of £30,000 starting from 1 October 2021 which she has included as a cost in her projections above.

On 1 May 2021 Wilma resigned from her position as marketing director for an international cycle manufacturer. Her gross salary for the period from 6 April 2021 to 1 May 2021 was £10,000. In 2020/21 her salary was £120,000. Wilma made no other capital disposals in 2019/20 but she does have a capital loss brought forward at 6 April 2020 of £5,000.

(b) **Gooch Food (June 2014)**

(37.5 mins)

Shar Gooch is a sole trader operating as Gooch Food. Shar's business manufactures ready meals for sale to supermarkets. Shar is married to Neeta and they have three children. Shar was born in Ganda, a non-EEA country where his parents still live. He came to the UK in January 2011 to set up the Gooch Food business and has been UK tax resident since then. Shar prepares and submits his own tax returns. Gooch Food has a 5 April year end.

You are a newly-qualified ICAEW Chartered Accountant and have recently started working as the accountant at Gooch Food. Shar gives you the following briefing:

I have just been to a meeting with a firm of business advisers called Tx3 who I may appoint as my tax advisers. I would like you to help me understand the advice given to me by Tx3. At the meeting, which was free-of-charge, the Tx3 adviser made the following tax planning proposals:

Proposal 1 – Make my wife Neeta a partner in Gooch Food

My business, Gooch Food, has made a taxable profit of £150,000 for the year ended 5 April 2021. This is after the deduction of a salary of £8,788 per annum paid to Neeta, my wife who works in product development at Gooch Food. The Tx3 adviser suggested I could save tax by making my wife a partner in the business. If I do this, it will be from 6 April 2022 and Neeta will receive a partnership profit share of £50,000. I expect Gooch Food profits to remain at £150,000 per annum for the foreseeable future before the deduction of Neeta's profit share.

Proposal 2 – Set up a discretionary trust for my granddaughter

As I have recently become a grandfather, I would like to set some assets aside for my granddaughter who was born last month. I have a portfolio of UK quoted shares with a market value of £300,000. I expect to receive dividends of £36,000 from these shares in the tax year 2021/22.

The Tx3 adviser suggested that I set up a discretionary trust and gift my portfolio of UK quoted shares to the trust making my granddaughter the beneficiary of the trust. Tx3 advised that this would ensure that no inheritance tax would be payable in respect of these shares when I die. My granddaughter does not need any money just yet but it would be good to set aside funds for her future education.

Proposal 3 – Paying key employees using an off-shore company

The Tx3 adviser proposed the following tax planning scheme which he claimed would save my business national insurance contributions (NIC) as it effectively 'hides' employees from HMRC. The scheme involves making key members of the Gooch Food management team redundant. These key employees, who each earn £100,000, would continue to work at Gooch Food but would become employees of an off-shore company called LK O/S which is managed by Tx3. LK O/S would invoice Gooch Food for the services of these employees together with a small administration fee.

LK O/S would then pay the salaries direct to the key employees without paying NIC or tax to HMRC on behalf of these employees.

Moving to Ganda

We also discussed my move to Ganda on 1 November 2021, the country where I was born. I will live there for 10 months and will set up a spice production factory in partnership with my brother. Although it will be difficult to be separated from my wife and children who will remain in the UK, I feel that the move is necessary to ensure that Gooch Food is supplied with good quality raw materials. I will be returning to the UK for the holidays; in December 2021 for four weeks and in the summer of 2022 for five weeks.

The Tx3 adviser told me that the move would save tax as I will not be taxed on any of the profit from Gooch Food after the date of my departure from the UK. Gooch Food's taxable profit for the year ending 5 April 2022 will be £150,000. My share of the partnership profits in Ganda for

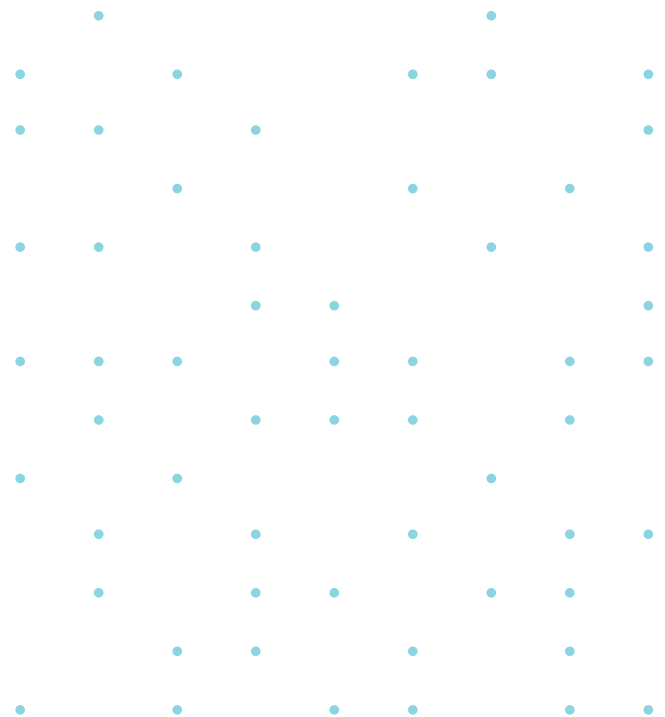
the period to 5 April 2022 will be £75,000. The Tx3 adviser told me that as long as the Ganda partnership profit share was not remitted to the UK, I would not pay any UK tax on these profits.

- 3 Explain to Shar and Neeta the tax and NIC implications of Neeta becoming a partner in Gooch Food (Proposal 1). Detailed calculations are not required.
- 4 Explain to Shar the inheritance tax implications of setting up a discretionary trust for his granddaughter (Proposal 2).
- 5 Advise Shar whether he should consider entering into the scheme to pay employees through the off-shore company LK O/S managed by Tx3 advisers (Proposal 3).
- 6 Determine whether Shar will be tax-resident in the UK in the tax years 2021/22 and 2022/23. Calculate the income tax payable by Shar in 2021/22 and identify any relevant claims or elections available, making appropriate recommendations on whether these claims or elections should be made.
- 7 Evaluate the ethical and professional issues for you in advising Shar and Neeta in respect of the tax planning proposals made by the Tx3 advisers.

Total: 25 marks



Answer Bank



(a) **Overseas aspects of personal taxation**
Scenario

The candidate is advising the owner, Bill, of a sole trader business on his retirement and sale to his daughter, Wilma. The question requires a good understanding of owner managed businesses and business start-ups. The candidate is replying initially to Bill and should use appropriate language and style. The candidate then is asked to prepare briefing notes for a forthcoming client meeting with Wilma and Jorge, Wilma's husband-to-be. The clients have some misperceptions about the tax implications of the sale and gift of some of his assets and the candidate must be able to identify these misconceptions and offer appropriate advice in a manner the client can understand.

Scenario

In this question the candidate is asked to advise on tax treatments which are intended to minimise or defer tax liabilities. The three proposals were: a partnership arrangement between the client and his spouse; a discretionary trust; and a scheme to pay employees through an offshore company. In this question the candidate needs to understand the interaction of taxes and to be able to discriminate between legitimate tax planning and tax evasion. The candidate is also required to consider the ethical implications of their own position as an ICAEW Chartered Accountant working for a company rather than in professional practice.

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